DOCKET FILE COPY ORIGINAL ORIGINAL

RECEIVED JAN 25 1995 FEDERAL COMMUNICATIONS COMMISSION OFFICE OF SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Implementation of Sections of	)	
the Cable Television Consumer	)	MM Docket No. 92-266
Protection and Competition	)	
Act of 1992: Rate Regulation	)	

PETITION FOR RECONSIDERATION

Home Shopping Network, Inc. ("HSN"), by its attorneys, respectfully petitions the Commission to reconsider one component of its recently announced "going forward" rules.[1/] Specifically, HSN requests the Commission to eliminate the requirement that cable operators that add video retailing or shop-at-home channels offset increased system costs which are recoverable from subscribers under the new "going-forward" rules with any sales commissions earned by the cable operators and paid by the shop-at-home channels. Because of their unique relationship with cable operators, shop-at-home channels (and other services that provide commissions to operators for the sale of products) are the only programmers affected by this particular rule. As a result, shop-at-home channels like HSN will find themselves at

1/ These rules were announced in Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, MM Docket No. 92-266, Sixth Order on Reconsideration, Fifth Report and Order, and Seventh Notice of Proposed Rulemaking, FCC 94-286 (adopted: November 10, 1994; released: November 18, 1994) (referred to herein as the "Going Forward Order").

No. of Copies rec'd 0+4
List ABCDE

a critical and unfair disadvantage vis-a-vis other types of programming for cable system capacity in an increasingly competitive market.

I. INTRODUCTION

HSN is in the business of electronic retailing, primarily through Home Shopping Club, Inc. ("HSC"), a wholly-owned subsidiary of HSN. HSC distributes three shop-at-home programming services: HSN 1, HSN 2, and HSN Spree. HSN 1 is distributed through cable television systems throughout the country; HSN 2 is carried by broadcast television stations and cable systems either redistributing those broadcast signals or cablecasting the satellite feed; HSN Spree is a part-time service carried both by cable systems and television broadcast stations.

HSN applauds the Commission's stated goal of avoiding judgments about the relative value to subscribers of various programming services.[2/] However, as described more fully below, the rule requiring offsets for shop-at-home commissions[3/], as currently written, will result in cable operators favoring one category of programming service over another. An operator that is faced with limited channel capacity will find that many of the incentives to add HSN will have been eliminated by the requirement that it offset channel charges under the going-forward

---

2/ See Going Forward Order, para. 82 ("The License Fee Reserve makes no judgment about the relative value to subscribers of high or low cost channels, but seeks to replicate the incentives operators would have to add channels in a competitive market, which accommodates both low and high cost services.")

3/ The offset rules will be codified at 47 C.F.R. § 76.922(e)(3)(ii).

rules against sales commissions which are received from shop-at-home services. While the Commission may not have intended to impose any judgments about the relative value of programming services, the offset rules, as currently drafted, will have the same impact. HSN, therefore, strongly urges the Commission to eliminate the requirement that operators offset allowable rate increases with sales commissions earned by the operator.

II. SALES COMMISSION OFFSETS UNFAIRLY AND IMPROPERLY DISADVANTAGE SHOP-AT-HOME PROGRAMMERS VIS-A-VIS ADVERTISER-SUPPORTED PROGRAMMING NETWORKS

The Commission's new rules require that, in calculating the allowable rate increase for an added channel, any revenues received from the programmer must be deducted from programming costs and then, to the extent revenues remain, from the $0.20 per channel adjustment. These offsets will apply on a channel-by-channel basis.

HSN would not oppose a rule offsetting programming costs with associated revenues if it were, in effect, programmer-neutral. But the sales commission offset requirement unfairly discriminates against certain programmers -- namely, shop-at-home services.[4/]

4/ Moreover, this rule contradicts the Commission's previous position on the issue, as stated in two letters from the Cable Services Bureau. As the Commission wrote: "[W]here, as in the case of HSN's shop-at-home services, payments are only made from the programmer to the operator . . . the operator may receive the benefit of the payment without decreasing or increasing charges to subscribers." Letter from Alexandra M. Wilson, Acting Chief, Cable Services Bureau to Peter H. Feinberg, Esq., May 6, 1994; accord Letter from Alexandra M. Wilson to Sue D. Blumenfeld, Esq. and Philip L. Verveer, Esq., May 6, 1994. (The Commission did not explain in (continued...)

Footnote 27 of the Going Forward Order provides that:

> commissions received by an operator from programmers will be treated as revenues received from programmers. Any commissions cable operators receive from programmers must, therefore, be netted against programming costs for the purpose of determining whether there has been an increase or decrease in the operator's external costs. After commission revenues have been deducted from programming costs, if there are still revenues remaining, such revenues shall be deducted from the per channel adjustment.[5]

Because there are no "programming costs," in the traditional sense, incurred by cable operators in carrying HSN, any and all sales commissions paid by HSN to its cable operator affiliates must be deducted from the $0.20 per channel adjustment factor. In marked contrast, a significant source of revenue received by cable operators for carrying many other services -- specifically, local advertising revenue -- does not have to be offset against the $0.20 increase.

Unlike HSN, traditional advertiser-supported programming networks generally provide cable operators with fixed, non-recoverable, amounts of local advertising availabilities ("avails"), typically in the range of two to three minutes per hour. These avails may be sold by the operator, or by the operator's agent, with the cable

---

4/ (...continued)
the Going Forward Order what changes have occurred in the past eight months to cause this apparent shift in position.) As the Commission has explained, the new going-forward rules seek to compensate operators for the costs incurred in providing additional channels. As a result, that policy should not affect the manner in which operators calculate external cost increases with respect to shop-at-home services. The Commission should clarify, therefore -- as it has done in the past -- that the sales commission offset rule does not apply to shop-at-home programming services.

5/ Going Forward Order, n. 27.

operator retaining all of the net revenue from such sale.[6] The Commission's decision to require an offset for sales commissions, but not for local advertising revenue, has the anomalous effect of punishing shop-at-home programming services as they become more successful.[7]

As a general rule, as programming services -- both traditional advertising-supported and shop-at-home -- become more attractive to subscribers and garner higher satisfaction levels, advertising revenues increase. However, under the new going forward rules, cable operators will be permitted to retain all of the increased revenues derived from local avails, without offset, but will be punished through higher offsets for increased sales commissions from shop-at-home services. In other words, as the value of a shop-at-home service increases to its subscribers, a cable operator will be asked to take an additional "hit" in terms of offsets. This result flatly contradicts the Commission's stated goal of programmer neutrality.

6/ Like HSN's sales commissions, local advertising availabilities are frequently the subject of intense negotiations between cable operators and programming networks, and are viewed by both parties as an important element of bargained for consideration in the decision to carry a particular network.

7/ HSN, however, does not believe that cable operators should be required to offset network costs by revenues derived from the sale of local advertising avails, for substantially the same reasons that sales commissions should not offset the per channel adjustment factor for home shopping services. (Moreover, doing so would effectively shut off cable as a viable distributor of local spot advertising, which makes little sense from a policy perspective that seeks to enhance competition in the marketplace.) HSN simply seeks parity with traditional advertiser-supported programmers in terms of cable operator incentives for carriage.

As the Commission notes in Paragraph 73 of the Going Forward Order, the per channel adjustment factor is designed to compensate the operator for its costs of adding the channel, plus a reasonable profit. The Commission estimates that $0.20 approximates the amount by which an operator in a hypothetically competitive environment would increase its rates upon adding a new programming channel.

The cost of adding a new channel to a cable system will not differ materially between a shop-at-home network and a more traditional advertiser-supported programming network. The cable operator incurs the same technical costs for adding the channel, and assumes the same risk that the channel will not be a success with subscribers. If either channel is a success, the operator receives comparable benefits: increased subscriber satisfaction, and additional revenue from the enhanced value of local avails and increased sales commissions. However, under the new rules, as each channel's popularity grows, it is only the shop-at-home channel that is penalized through increased offsets, not the traditional advertiser-supported channel.

As a result, what the Commission contemplated as an even-handed incentive program to increase programming diversity on cable systems will ultimately drive operators to favor advertiser-supported networks over shop-at-home formats. That message is already being heard loud and clear by cable operators, and has been the subject of numerous conversations between HSN and its potential cable operator customers. When combined with the procedural difficulties of complying with the sales commission offset rule, the effect on cable operators has been predictable, and discouraging.

III. THE COSTS OF COMPLYING WITH THE SALES COMMISSION OFFSET RULE WILL SIGNIFICANTLY DISADVANTAGE SHOP-AT-HOME PROGRAMMERS VIS-A-VIS TRADITIONAL ADVERTISING-SUPPORTED NETWORKS

The Commission's brief discussion of the sales commission offset rule in footnote 27 of the Going Forward Report gives no hint of the enormous complexity and costs associated with complying with this rule, two factors that will not affect an operator's decision to carry traditional advertising-supported program services. Cable operators, already facing complex rate regulations, are simply not going to add shop-at-home networks if the cost of complying with the offset rules is significantly higher than for traditional program services. The sheer mechanics of calculating and implementing the sales commission offset will be more than enough to dampen, if not extinguish, the most enthusiastic cable operator's spirit for carrying these "useful shop-at-home services."[8]

Extraordinarily, there is no discussion in the Going Forward Order as to how the sales commission offset rule will be implemented. As any operator will testify, the calculation of sales commissions is itself a complex task, given the potential for returns, credits, and other fulfillment related factors. If an operator carries more than one shop-at-home channel, these difficulties may be compounded by the potentially different payment schedules on which these businesses may operate.

In stark contrast, a cable operator faces significantly less complexity when making the decision whether or not to carry a traditional advertiser-supported

---

8/ See Letter from Alexandra M. Wilson, Acting Chief, Cable Services Bureau to Peter H. Feinberg, Esq., May 6, 1994.

network. The operator typically knows the associated programming costs of adding the channel, often for a period of at least five years, and can even calculate any future marketing or launch support revenues to which the system may be entitled. While dealing with regulatory complexity has become a staple of a cable operator's existence, HSN firmly believes that no amount of perceived subscriber value can overcome the daunting prospect of complying with this rule. As a result, the Commission's goal that the "new going-forward rules for channel additions should benefit consumers by increasing their viewing options on CPSTs, while avoiding unreasonable price increases for those tiers[,]" will remain substantially unfulfilled, unless the sales commission offset requirement is eliminated.

IV. CONCLUSION

As the Commission undoubtedly appreciates, when dealing with a complex, multi-faceted industry, no regulatory scheme will ever perfectly replicate marketplace conditions; consequently, when marketplace-driven solutions present themselves, regulators should allow them to govern the process. In particular, the Commission should be extremely cautious as it attempts to reproduce incentives that, in a hypothetically competitive environment, will cause cable operators to add programming services to systems with already limited channel capacity. As the Commission pushes and pulls various economic levers in an attempt to replicate this environment, it must be careful not to prejudice, directly or indirectly, the purchasing decisions of those it regulates or to distort the programming marketplace in which services compete for limited channel capacity. HSN respectfully submits that the Commission, in enacting the sales commission offset rule, has pulled one lever too many.

Laudably, the Commission has stated a policy goal of maintaining programmer neutrality in the going-forward rules. HSN urges the Commission to follow through with this plan by eliminating "transaction-based" dis-incentives that will seriously disadvantage, if not cripple, shop-at-home networks. Because cable operators have already interpreted the Commission's per channel adjustment factor rules as discouraging the addition of shop-at-home services, HSN urges the Commission to move quickly to rectify the situation. The Commission should, as it has done previously, clarify that the sales commission offset rule does not apply to shop-at-home or video retailing programming services.

For the above stated reasons, HSN respectfully requests the Commission to reconsider its Going Forward Order, and eliminate the sales commission offset requirement.

Respectfully submitted,

HOME SHOPPING NETWORK, INC.

By: ____________________

Brenda L. Fox
Peter H. Feinberg
Michael J. Pierce
DOW, LOHNES & ALBERTSON
1255 Twenty-Third Street, N.W.
Suite 500
Washington, D.C. 20037
(202) 857-2500

January 5, 1995

Its Attorneys